7535-01-U

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 704

RIN 3133- AD58

Corporate Credit Unions

AGENCY: National Credit Union Administration (NCUA).

ACTION: Advance notice of proposed rulemaking and request for comment (ANPR).

SUMMARY: In the light of current economic circumstances affecting the U.S. economy and, in particular, the financial sector, NCUA is evaluating and reconsidering the role corporate credit unions currently play in the credit union system, including corporates' membership structure, size, and types of services they offer. NCUA is also considering whether to amend its regulation governing corporate credit unions to clarify or revise current provisions, including those related to: capital; permissible investments; management of credit risk and

liquidity; and corporate governance. NCUA seeks comment on these issues and any others commenters think NCUA should consider.

DATES: Comments must be received on or before [INSERT DATE THAT IS SIXTY DAYS FROM DATE OF PUBLICATION IN THE FEDERAL REGISTER].

ADDRESSES: You may submit comments by any of the following methods (**Please send comments by one method only**):

- Federal eRulemaking Portal: **http://www.regulations.gov**. Follow the instructions for submitting comments.
- NCUA Web Site: **http://www.ncua.gov/RegulationsOpinionsLaws/proposed_regs/proposed_regs.html**. Follow the instructions for submitting comments.
- E-mail: Address to **regcomments@ncua.gov.** Include "[Your name] – Comments on Advanced Notice of Proposed Rulemaking for Part 704" in the e-mail subject line.
- Fax: (703) 518-6319. Use the subject line described above for e-mail.
- Mail: Address to Mary Rupp, Secretary of the Board, National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314-3428.
- Hand Delivery/Courier: Same as mail address.

PUBLIC INSPECTION: All public comments are available on the agency's website at http://www.ncua.gov/RegulationsOpinionsLaws/comments as submitted, except as may not be possible for technical reasons. Public comments will not be edited to remove any identifying or contact information. Paper copies of comments may be inspected in NCUA's law library at 1775 Duke Street, Alexandria, Virginia 22314, by appointment weekdays between 9:00 a.m. and 3:00 p.m. To make an appointment, call (703) 518-6540 or send an e-mail to OGCMail@ncua.gov.

FOR FURTHER INFORMATION CONTACT: Ross Kendall, Trial Attorney, Office of General Counsel, at the above address or telephone: (703) 518-6540, or David Shetler, Senior Corporate Program Specialist, at the above address or telephone (703) 518-6640.

SUPPLEMENTARY INFORMATION:

A. Background.

The Federal Credit Union Act (Act) authorizes natural person federal credit unions (FCUs) to invest in shares or deposits of any central credit union (corporate credit union). 12 U.S.C. 1757(7)(G). A corporate credit union is an organization, chartered under the Act or under applicable state law as a credit union that receives shares from and provides loan and other services primarily to other credit unions. 12 CFR 704.2. Historically, corporate credit unions have fulfilled an important role in the credit union industry and have provided credit unions with payment and clearing services, including access to wire transfer facilities and automated clearing house transactions. Corporate credit unions have also provided investment services, enabling smaller credit unions to achieve economies of scale and access to greater market returns otherwise unavailable to them. Corporate credit unions have been an important source of liquidity for credit unions through short and medium term credit facilities, and have served as agents on behalf of NCUA's Central Liquidity Facility (CLF) in connection with loans funded by the CLF. Corporate credit unions have also provided other operational services, such as coin and currency services and safekeeping of investments.

There are currently twenty-eight corporate credit unions serving the nation's approximately 7,900 credit unions. As with all credit unions, corporate credit unions are organized as cooperatives, owned by their members and responsive to their needs, enabling members to receive access to necessary products and services at affordable rates. They provide a level of expertise and market presence that would be unavailable to most of their members if required to rely solely on their own resources.

B. Current Economic Climate and Remedial Measures Taken.

Over the last year, many corporate credit unions have experienced a dramatic reduction in the value of their investment portfolios. These reductions, coupled with, in some cases, the virtual freeze-up of the market for trading in certain types of investment securities, have undermined the stability of the corporate credit union system. Simultaneously with the issuance of this Advance Notice of

Proposed Rulemaking, which is designed to identify issues that may have contributed to the current state of affairs and to solicit comment and ideas on how to address them as the industry moves ahead, the NCUA Board has taken several actions with a more immediate, remedial impact, designed to stabilize the industry and maintain confidence in the corporate system. These actions include the following:

- An infusion of $1 billion in capital into U.S. Central Federal Credit Union, the corporate system's wholesale credit union, by the National Credit Union Share Insurance Fund (NCUSIF); and
- A temporary NCUSIF guarantee of all member shares, for any corporate credit union that decides to participate in a voluntary guarantee program offered by NCUA.

The Board believes these extraordinary measures, which are mandated by the exigent economic conditions affecting the country, will help stabilize the corporate credit union system and enable credit unions return to their primary mandate, which is to provide affordable financial services to their members. The Board believes that identifying and addressing the issues discussed in this ANPR will help continue to assure stability and confidence in the corporate credit union system in the future.

C. Issues for Consideration.

Notwithstanding the successful role that corporates have played in the credit union sector, events of recent months have highlighted several areas in which re-evaluation is appropriate and necessary. As set out more fully below, these include some fundamental aspects concerning the structure, role and services offered by corporate credit unions to the credit union industry.

1. **The Role of Corporates in the Credit Union System.**

Recent events have highlighted structural vulnerabilities in the corporate credit union system. NCUA is considering whether comprehensive changes to the structure of the corporate system are warranted. Possible approaches the agency is considering include eliminating the second or wholesale tier from the corporate system, modifying the level of required capital, isolating payment services from the risks associated with other lines of business, determining which product and service offerings are appropriate for corporates, requiring a restructure of corporate boards, and tightening or eliminating the expanded investment authority that is currently available to corporates.

Payment system. Some of the questions and issues arising in this context, on which the Board is seeking comment, include matters such as whether payment system services should be isolated from other services to separate the risks. If so, what is the best structure for isolating these services from other business risks? Specific comment is solicited concerning whether, for example, it would be better to establish a charter for corporate credit unions whereby a corporate's authority is strictly limited to operating a payment system, with no authority to engage in other services, such as term or structured investments. Additionally, a separate charter may be available for corporate credit unions that want to engage in providing investment services. Another alternative would be for NCUA to establish distinct capital requirements for payment systems risk and the risks of other corporate services. NCUA could also require that a legal and operational firewall be established between payment system services and other services. In connection with this topic, comment is also sought on the question of whether there is sufficient earnings potential in offering payment systems to support a limited business model that is restricted to payment systems services only.

For credit unions that use Corporates for payment processing and transaction settlements, the current system functions fine. Smaller credit unions probably could not survive without this valuable service and the expertise of Corporate personnel handling this function. This function would be cost prohibitive without the accumulation of larger transaction volumes. Corporates provide the mechanism for this aggregation. CDC FCU recognizes these services are readily available outside our industry through intermediary banks and other financial institution servicers.

As to maintaining separate charters for the express purpose of performing payment functions for natural person credit unions, it is our management's conclusion that such a charter would not be sustainable given current business models available. Management is persuaded that a corporate credit union should have the flexibility in its charter to also offer liquidity and investment products and services for its members. That model should have the flexibility to offer the various kinds of services member credit unions desire and are willing to support through capital ownership.

Liquidity and liquidity management. Historically, the primary role of corporate credit unions has been to provide and ensure liquidity. Corporate investments were made with an eye towards ensuring funds would be available to meet members' short-term liquidity needs. Recent events underscore the need to assure a corporate properly considers its investment position relative to its cash flow needs. The Board recognizes and understands that providing liquidity for the credit union system is one of the principal purposes of the corporate credit union network. One question for consideration and comment is whether liquidity ought to be considered a core service of the corporate system, and if so, what steps should be taken, and by whom, to preserve and strengthen corporates' ability to offer that service? For example, should NCUA consider limiting a corporate's ability to offer other specific types of products and services in order to preserve and defend the liquidity function? What specific types of products and services should corporates be authorized to provide?

NCUA is considering additional cash flow measuring requirements to assist corporates in achieving and maintaining proper liquidity management. In this respect, comment is specifically solicited on the question of whether NCUA should add aggregate cash flow duration limitations to Part 704. If so, commenters are invited to describe how this requirement should be structured, and also to identify how such limitations would benefit liquidity management. Finally, comment is solicited on the question of what cash flow duration limits would be appropriate for corporate credit unions, particularly in an evolving interest rate market with previously unseen credit risk spreads.

It is the conclusion of CDC FCU management that liquidity services should be a core function of the Corporate credit union network. CDC FCU relies on the support of the Corporates in providing a Line of Credit for its short and long term needs. As Corporates have sought additional funding from other reliable sources, such as the Federal Home Loan Banks (FHLB), it is management's conclusion that natural person credit unions should also pursue these outside sources of liquidity from other institutions (i.e. bank lending from reverse re-purchase security agreements, Federal Reserve discount window, etc.).

It is management's position that the NCUA should take requisite steps to preserve and defend the ability of Corporates to provide liquidity to member credit unions. However, that assumes the agency has the expertise on staff with sufficient knowledge and experience to know how and when to step in to preserve and defend the ability to insure adequate liquidity for Corporates as well as natural person credit unions.

As to the question regarding products and services to provide liquidity, management asserts that a broad range of products should be allowed for Corporates to accomplish this service. Products such as reverse re-purchase agreements, Lines of Credit, waivers granted for natural person credit unions seeking Lines of Credit with the FHLB, assistance in accessing the Fed discount window, offering of time deposits and the ability to purchase natural person credit union assets for the purpose of securitizing and selling in the Capital Markets should be permitted within a reasonable risk tolerance.

It is management's conclusion that cash flow measuring requirements should be required as part of good cash flow management by the Corporate risk management personnel to the extent they deem necessary. It is management's position that NCUA should NOT add aggregate cash flow duration limitations to Part 704. This addition would only lead to further restrictions by Corporate management in its liquidity management by managing to a regulatory requirement rather than the needs of the industry. The Agency should possess capable examiners to monitor cash flow needs of the Corporates. If warranted, examiners should raise issues of cash flow duration abnormalities and make appropriate inquiries of Corporate management. If Corporate management's plan is sound, current practices should be allowed to continue, if not, the Agency should exercise its authority to remedy the issue under existing rules.

Field of Membership Issues. NCUA also seeks comment on whether and how to restructure the corporate credit union system. For example, despite its intention of fostering competition, NCUA's decision to allow corporates to have national fields of membership (FOMs) may have resulted in significant, and unforeseen, risk taking. For example, corporates have competed with each other to offer higher rates, and have done so through the accretion of credit and marketability risks. To address this development, should the agency return to defined FOMs, for example, state or regional FOMs?

CDC FCU management is split on this issue. Defined fields of membership may be an acceptable compromise given the complexity of existing FOMs granted by the Agency. The FHLB membership structure may be a good model or that of Federal Farm Credit Banks. In all cases, member credit unions should be required to maintain capital in their Corporate(s).

Expanded Investment Authority. At present, Part 704 provides for an option by which corporates meeting certain criteria can qualify for expanded investment authority. For example, a corporate meeting the criteria set out under Part One of the expanded authority is allowed to purchase investments with relatively lower credit ratings than otherwise permissible under the rule. NCUA seeks comment, first, as to whether the need for expanded authorities continues to exist. If so, should NCUA modify the procedures and qualifications, such as higher capital standards, by which corporates currently qualify for expanded authorities? If so, what should the new standards be? Should NCUA reduce the expanded authorities available? If so, which ones? Alternatively, should any of the limits in existing expanded authorities be reduced or increased? If so, which ones? Once granted, should NCUA require periodic requalification for expanded authorities? If so, what should be the timeframe?

Yes, there is a continued need for expanded authorities. It is clear that Corporates need to raise their amount of required capital. It has become clear that the appetite for higher risk investments in Corporates to achieve certain target returns was too high for the existing capital level. Some tolerance for higher risk for lower quality investments was perhaps justifiable and if higher capital requirements had been in place for several years, maybe even acceptable. Management recognizes that is not the case now, and to continue to rely on regulatory edicts as a cure is not the answer. Our industry is in the business of risk and, unfortunately, learned the most about risk tolerance when the industry could least afford it. Therefore, it is management's conclusion that the NCUA should modify procedures and qualifications as they pertain to required capital levels in Corporate credit unions but not tied to expanded investment authorities. In general raising capital requirements is a good idea, restricting investment authority based on capital levels destroys the flexibility of management to make these kinds of informed decisions based upon their own analysis. Concerns should continue to be raised by the regulator where appropriate. Evaluation of the Corporates risk management should still be in the hands of the Board not the regulator.

If periodic qualifications must exist, then a reasonable period (3-5 years) should be established. In our opinion, annually is too onerous a regulatory burden.

Further, it should be mentioned that highly skilled, thoughtful and knowledgeable Corporate personnel should be managing these important issues along with adequate oversight from the regulators. Corporate long term success depends on these crucial characteristics.

Structure; two-tiered system. Over time, the corporate system has evolved into two tiers: a retail network of corporates that provide products and services to natural person credit unions, and a single, wholesale corporate that exclusively services the retail corporates. NCUA solicits comment about whether the two-tier corporate system in its current form meets the needs of credit unions. Specifically, NCUA seeks input from commenters about whether there is a continuing need for a wholesale corporate credit union. If so, what should be its primary role? Should there be a differentiation in powers and authorities between retail and wholesale corporates? In considering these issues, commenters are specifically asked to consider whether the current configuration results in the inappropriate transfer of risk from the retail corporates to the wholesale corporate. Commenters should also address whether, assuming the two-tiered system is retained, capital requirements and risk measurement criteria (e.g., NEV volatility), as well as the range of permissible investments, for the wholesale corporate credit union should be different from those requirements that apply to a retail corporate credit union.

In the opinion of management, there is a continuing need for a wholesale Corporate Credit Union system. Going forward, there appears to be a need for a Corporate Credit Union to access the capital markets. However, the structure will need to be changed. Consolidated into regional Corporates of geographic design, would lead to fewer Corporates with greatly increased economies of scale and a significant reduction in operating costs. Currently, access to the capital markets consists of traditional borrowing, investing and perhaps lending activities for liquidity management purposes. These activities need to continue in the future. Added to these traditional activities should be a department that securitizes assets from credit unions and sells these credit union assets (serviced by the originating credit union) in the capital markets as another liquidity option much like the FHLB funds its balance sheet. This enables the industry to have another avenue for liquidity, continual contact with its member, and leverage its penchant for great underwriting practices. This will require a knowledge base that does not currently exist in credit unions, but is readily available from displaced workers from the investment community. This will also require a step-up in Agency expertise at the supervisory and examiner level to understand, monitor, report and regulate these essential services.

Perhaps there should be a differential in powers and authorities of wholesale Corporates, assuming the preceding paragraph's model is adopted. However, it is the conviction of this management team that this could be accomplished within the same Corporate charter as a retail Corporate. However, management recognizes this could be accomplished with a dual chartering system.

Pertaining to the transfer of risk, it is the opinion of this management team that there is not an inappropriate transfer of risk prevalent in the current system. There was a failure to properly recognize, assess and report on that level of risk by the Corporates investment management team. There was an equal failure on the Agency's part to discover, assess and reveal the inappropriate level of risk being assumed by the Corporates. The risk could have been avoided or certainly mitigated if the Corporates and Agency were attentive to the risk issue.

In management's view, there is no need to require two different types of capital and risk measurements to Corporate Credit Unions. However, the risk must be managed in such a manner to create adequate capital to support the risk assumed by the Corporate, regardless of whether it is wholesale or retail. Further, credit unions need to be prepared to ante-up the amount of capital necessary to assure adequate capital levels for the risk involved, otherwise they will fail.

2. Corporate Capital.

NCUA is considering revising various definitions and standards for determining appropriate capital requirements for corporate credit unions. For example, the agency could establish a new required capital ratio consisting only of core capital excluding membership capital accounts as a component of regulatory capital; the agency could also determine to increase the required capital ratio to more than four percent. The agency could also establish a new ratio based on risk-weighted asset classifications, which could include some form of membership capital. These changes would bring the corporate capital requirements more into line with standards applied by other federal financial regulators, such as the Comptroller of the Currency and the Federal Deposit Insurance Corporation (recognizing, however, that there are other accounting differences that apply with respect to the calculation of regulatory capital for banks). Another issue under consideration is whether to require a certain level of contributed capital from any natural person credit union seeking either membership or services from a corporate.

Core capital. The Board is considering several issues relating to the agency's approach to core capital (i.e., the traditional "tier one capital" definition as used by the several federal financial institution regulators). Under the current rule, core capital is defined as retained earnings plus paid-in capital. 12 CFR 704.2. Comment is invited concerning whether NCUA should establish a new capital ratio that corporates must meet consisting only of core capital, and if so, what would be the appropriate level to require. Commenters should offer their view concerning what actions are necessary to enable corporates to attain a sufficient core capital ratio as described above, as well as their thought about what would be an appropriate time frame for corporates to attain sufficient capital. The Board invites comment also on the question of what is the appropriate method to measure core capital given the significant fluctuation in corporate assets that occur. Commenters are invited to offer their view on the correct degree of emphasis that ought to be placed on generating core capital through undivided earnings. Finally, NCUA Is considering whether to require that a corporate limit its services only to members maintaining contributed core capital with the corporate. Commenters are invited to react to that idea, and to offer any other suggestions or comments relative to the issue of core capital for corporates.

CDC FCU management concedes that under the current circumstances capital has proven to be inadequate for Corporate Credit Unions. However, on some level, management recognizes that capital would have been adequate under the current structure. It is our conclusion there was a failure in the Corporate's management to properly evaluate the risk that investment portfolios retained and it is apparent the Agency was ill equipped with the expertise to recognize and expose these risks as well. Management also acknowledges culpability on the part of rating agencies. It is also our management's conclusion that capital is currently inadequate at the Corporate level and should have capital requirements raised. Whether to use other banking Agencies as a barometer of capital measurement for credit unions may not be such a good idea either considering that their capital issues are quite staggering as well and two inadequate models does not equal one good one. Our management's preference is for Corporates to build sustained capital through undivided earnings and an appropriate level of perpetual Paid-In-Capital supported by some type subordinated capital certificate. Void of building capital through the selling of shares, this structure best supports the cooperative network. CDC FCU management thinks this methodology best supports the core capital definition and should be tied into Basel II accords. An appropriate time frame for restoring this capital should be at least five years up to seven years depending on the asset size of the Corporate.

It is the conclusion of management that users of Corporate services should be capital paying members.

Membership capital. The Board is also considering several issues involving membership capital. 12 CFR 704.3(b). Issues under consideration and for which comment is sought include whether NCUA should continue to allow membership capital in its current configuration, or should the agency eliminate or modify certain features, such as the adjustment feature, so that membership capital meets the traditionally accepted definition of tier two capital. Other questions include whether to tie adjusted balance requirements, as set out currently in §704.3(b)(8), only to assets, as well as whether to impose limits on the frequency of adjustments. The agency is considering whether to require that any attempted reduction in membership capital based on downward adjustment automatically result in the account being placed on notice, within the meaning of current §704.3(b)(3), so that only a delayed payout after the three-year notice expires is permissible. Comment is also sought on whether to require that any withdrawal of membership capital be conditioned on the corporate's ability to meet all applicable capital requirements following withdrawal. Comment is invited on all these issues and on any revisions NCUA should consider for the definition and operation of membership capital.

The current capital structure appears to management to be adequate. With the correct risk management structure in place by the Corporates and an Agency that understands the transactional and risk nature of Corporates and how to identify adverse risk signs and report it to Corporate and Agency management teams, the Corporates should be able to withstand future financial challenges.

Further, Corporate capital should be allowed to be withdrawn immediately, provided there are acceptable purchasers of the withdrawn capital instruments. Otherwise, application can be made and withdrawal allowed following a specified period of time (three years suggested) and held by the Corporate as a Treasury purchased capital instrument.

Risk-based capital and contributed capital requirements. Comment is solicited with respect to the following issues pertaining to risk-based capital and contributed capital requirements. Should NCUA consider risk-based capital for corporates consistent with that currently required of other federally regulated financial institutions? What regulatory and statutory changes, if any, would be required to effectuate such a change? Should a natural person credit union be required to maintain a contributed capital account with its corporate as a prerequisite to obtaining services from the corporate? Should contributed capital be calculated as a function of share balances maintained with the corporate? What about using asset size?

It is appropriate for Corporates to be assessed capital requirements on a risk-weighted basis. Again management cautions the Agency not to heavily rely on the requirements of other Agencies for other banking and thrift institutions. The uniqueness of credit unions and the cooperative movement could be lost in the haste to make changes for changes sake. It does flow logically that risk based capital requirements are the way to go with the Corporate environment. Assessments can be made and refined of the risk based assets and liabilities that can lead to fair and equitable capital requirements for each surviving Corporate. These could be tracked with some modifications to the current call reporting and examination system and adjusted every other year end. A natural person credit union should not necessarily be required to become a capital contributing member in order to have transactions performed by different Corporate Credit Unions. Many natural person credit unions have, as a part of their diversification strategy, placed excess liquidity within the Corporate network system in an effort to keep the funds “in the family”. Requiring a membership capital contribution may deter natural person credit unions from keeping liquidity within the Corporate network system thus defeating the purpose of our cooperative efforts. It is our conviction that membership should be required in a Corporate Credit Union in order to transact business within the system. However, non-members of each Corporate should not expect the same pricing privileges as members.

3. Permissible Investments.

NCUA is considering whether the corporate investment authorities should be constrained or restricted. Presently, corporates have the authority to purchase and hold investments that would not be permissible for natural person FCU members under Part 703 (or, in some cases, outside of what is authorized for a state chartered credit union). This increases a corporate member's exposure to these risks commensurate with their level of investment in the corporate. Questions on which comment is solicited in this context include whether NCUA should limit corporate credit union investment authorities to those allowed for natural person credit unions. NCUA is also considering whether to prohibit certain categories of, or specific, investments, for example: collateralized debt obligations (CDOs), net interest margin securities (NIMs), and subprime and Alt-A asset-backed securities. Comment is solicited on that issue, as well as on whether NCUA should modify existing permissibility or prohibitions for investments.

Corporate Credit Unions, like natural person credit unions, are in the business of managing risk. Therefore, the amount of risk these financial institutions should be willing to take is dependent upon board policy for risk tolerances, staff expertise in dealing with various kinds of financial instruments, and abiding within capital restraints. All investments that fit within the above mentioned framework should be allowed. The regulating Agency, if it has concerns, should voice them. The Agency must have employees on staff with capital market experience commensurate with the risk being assumed by the regulated entity. Mitigating signs that some Corporates saw which motivated them to sell their positions or avoid these risky investments altogether, were either not recognized or ignored by these large Corporates and the Agency. So the answer is permissible investments should be managed and regulated properly!

4. Credit Risk Management.

The reliability of credit ratings for investments has become more questionable in light of events in the financial industry and the current absence of regulatory oversight for rating organizations. Consequently, NCUA is considering curbing the extent to which a corporate may rely on credit ratings provided by Nationally Recognized Statistical Rating Organizations (NRSROs). Comment is requested on whether NCUA should require more than one rating for an investment, or require that the lowest rating meet the minimum rating requirements of Part 704. NCUA also solicits comment on whether to require additional stress modeling tools in the regulation to enhance credit risk management.

Several specific aspects of this issue are under consideration, for which comment is solicited, including whether Part 704 should be revised to lessen the reliance on NRSRO ratings. Commenters are invited to identify any other changes they believe may be prudent to help assure adequate management of credit risk. In this respect, commenters should consider whether Part 704 should be revised to provide specific concentration limits, including sector and obligor limits. If so, what specific limits would be appropriate for corporate credit unions? Comments are also solicited on the question of whether corporates should be required to obtain independent evaluations of credit risk in their investment portfolios. If so, what would be appropriate standards for these contractors? Another issue under consideration is whether corporates should be required to test sensitivities to credit spread widening, and if so, what standards should apply to that effort.

The question of whether to require more than one rating from an NRSRO is a perplexing one. On the one hand, that industry has been replete with self-serving optimistic ratings and on the other hand, one NRSRO may be too optimistic while another is too pessimistic. Management tends to think that more is better in this case. Three is probably the most reliable with the two extremes eliminated. Regarding the requirement of additional stress modeling tools in regulations to enhance credit risk management, the answer is yes. Relative to concentration limits, the management of CDC FCU believes that concentration risk should be managed and regulated properly, both of which have been lacking at the

Corporate Credit Unions and the Agency. Sector limits should be set by Board policy, monitored and managed. For example, emerging market investments, sub-prime lending and high risk Structured-Investment-Vehicles (SIV) should be strictly limited or eliminated from investment options. Independent evaluations of credit risk should be sought when there is disagreement regarding the safety and soundness of an instrument or classified group of investments. Certainly, independent verifications should be obtained on any identified group of impaired investments. It makes good sense that independent verifiers selected should come from a pool of verifiers not connected in any way with instruments that are being evaluated.

5. Asset Liability Management.

In a previous version of its corporate rule, NCUA required corporate credit unions to perform net interest income modeling and stress testing. Because one of the problems leading to the current market dislocation is a widening of credit spreads, the agency is considering re-instating this requirement. Alternatively, the agency may consider some form of mandatory modeling and testing of credit spread increases. Comment is solicited on whether NCUA should require corporates to use monitoring tools to identify these types of trends, including specifically comments about tangible benefits, if any, that would flow from these types of modeling requirements.

Management concurs with this requirement. Further, management believes any entities engaged in performing stress tests on the Corporate's portfolios should not be the same entity through which the security was purchased.

6. Corporate Governance.

The sophistication and far-reaching impact of corporate activities requires a governing board with appropriate knowledge and expertise. NCUA is considering minimum standards for directors that would require a director possess an appropriate level of experience and independence. The agency is also considering term limits, allowing compensation for corporate directors, and requiring greater transparency for executive compensation. Comment is sought on all these issues.

In addition, commenters are invited to respond to the question of whether or not the current structure of retail and wholesale corporate credit union boards is appropriate given the corporate business model. Should NCUA establish more stringent minimum qualifications and training requirements for individuals serving as corporate credit union directors? If so, what should the minimum qualifications be? NCUA is also considering whether to establish a category of "outside director," i.e., persons who are not officers of that corporate, officers of member natural person credit unions, and/or individuals from entirely outside the credit union industry. Commenters should offer their view on whether that approach is wise, and, if so whether NCUA should require that corporates select some minimum number of outside directors for their boards. Should a wholesale corporate credit union be required to have some directors from natural person credit unions? Comment is sought on whether NCUA should impose term limits on corporate directors, and, if so, what the maximum term should be. Comment is also sought on whether corporate directors should be compensated, and, if so, whether such compensation should be limited to outside directors only. Another issue under consideration, for which reaction from commenters is sought, is whether NCUA should allow members of corporate credit unions greater access to salary and benefit information for senior management.

Management of CDC FCU agrees there should be an appropriate level of expertise demonstrated on the part of Corporate Board members. Proposed Board members should be required to furnish a biographical sketch that supports a certain level of expertise (and subject to verification), whether it is in ALM, supervisory evaluations or other Board disciplines. Management agrees there should be term limits imposed. It is recommended terms should be limited to three, three year terms for any position on the respective Board. It is management's view there should not be outside directors. What an indictment against our industry that we cannot find qualified Board members from more than 8,000 credit unions! There are many highly qualified senior managers in our system that can perform at a high level in multiple disciplines and certainly without compensation other than covering cost of time and travel expenses. What an insult to credit unions if our industry has to turn to those outside our movement for direction and charting our strategic destiny! Should outside directors become necessary, one could certainly make the case for a single regulator, which we strongly do not advocate.

Request for Comments.

The NCUA Board invites comment on any of the issues discussed above including specifically if NCUA's regulations should be amended to address the issues discussed in this ANPR. NCUA also welcomes comment on any other relevant issues pertaining to corporate credit unions that have not been addressed in this ANPR.

It is the conviction of management there must be some consolidation for wholesale credit unions that have access to the capital markets. That may mean preserving US Central FCU for the purpose of acquiring credit union assets, securitizing and selling them in the capital markets, and creating liquidity while retaining the member relationship through servicing the loan. This model is much like the Federal Farm Credit Banks and the Federal Home Loan Bank model.

The best model appears to be one, retail Corporate Credit Union per region which would offer a full line of settlement and payment related services. Still, a three tiered system, but one that functions much better.

One item that deserves some thought is the negative long term impact the failure of the Corporates and the Agency will have upon smaller natural person credit unions. There will be many credit unions that will not survive this restructuring; therefore, it will become imperative for the strong to preserve the membership of the weaker credit unions. This can be accomplished through utilizing existing Corporate Credit Unions as holding companies for smaller credit unions. These Corporates could perform some of the shared functions that, individually, smaller credit unions cannot afford (marketing, internal & external auditing, compliance work, etc.). Under this arrangement, the Corporate would be responsible for filing a consolidated 990, 5300, W2s, a consolidated set of audited financial statements and all other regulatory filing requirements. The individual credit unions would retain their unique names and existing Fields of Membership. The staffs would remain basically the same with some elimination of services individual credit unions may have undertaken themselves (human resources, internal auditing, marketing, IT, etc.). Members will be served by familiar member service representatives and perhaps not feel abandoned by events they could not control. Over time, cost savings could be gained by consolidated services (IT, marketing, human resources, supplies, etc.), reduced personnel and benefit costs, and streamlined delivery of products and services. Cumbersome at first and perhaps a great way to preserve the personal service members have come to expect from their credit union. It will certainly be worth investigating.

By the National Credit Union Administration Board on January 28, 2009.

Mary F. Rupp
Secretary of the Board